SUMMARY of COOPERATIVE CASES

FARMER COOPERATIVE SERVICE
U. S. DEPARTMENT OF AGRICULTURE
WASHINGTON, D. C.

SUMMARY NO. 61 SEPTEMBER 1954

UNITED STATES DEPARTMENT OF AGRICULTURE
FARMER COOPERATIVE SERVICE
WASHINGTON, D.C.

SUMMARY OF COOPERATIVE CASES

*

* *

Prepared by

RAYMOND J. MISCHLER, *Attorney*
OFFICE OF THE SOLICITOR, U.S.D.A.

SUMMARY NO. 61

SEPTEMBER 1954

TABLE OF CONTENTS

The comments on cases reviewed herein represent the personal opinion of the author and not necessarily the official views of the Department of Agriculture.

INITIAL DECISION MADE IN TENNESSEE BURLEY TOBACCO GROWERS' ASSOCIATION CASE

(Ivan Range v. Tennessee Burley Tobacco Growers' Ass'n,
Ch. Court Greene County, decided August 24, 1954)

Because of the general interest in this case, the memorandum decision of Judge Geo. R. Shepherd is being set forth in full. The court held, in effect, that the members of the association should be given the option of having the net gains from the sale of tobacco placed under C.C.C. loan either paid to them in cash or invested in the capital of the association.

"The Tennessee Burley Tobacco Growers' Association was organized under the co-operative marketing laws of Tennessee on August 25th, 1941, and since that time has been active regularly and continuously. It is a non-profit association without capital stock. The purpose of the Tennessee Burley Tobacco Growers' Association as originally stated was:

> "'To engage in any activity in connection with the marketing or selling of the agricultural products of its members, or with the harvesting, preserving, drying, processing, canning, packing, grading, storing, handling, shipping or utilization thereof or the manufacturing or marketing of the by-products thereof; or in connection with the manufacturing, selling or supplying to its members of machinery, equipment or supplies; or in the financing of the above enumerated activities; or in any one or more of the activities specified herein.'

"The chief work of the Tennessee Burley Tobacco Growers' Association or its prime function since its organization has been to administer the loan support program as agent of the Commodity Credit Corporation of the federal government for the benefit of the farmers of Tennessee. At the time of the filing of this suit there were approximately 76,000 members of the Tennessee Burley Tobacco Growers' Association. H. S. Duncan was and is at present and has for some time prior to the filing of the suit been secretary-treasurer and general manager of the association. There are eleven directors of the association. The Commodity Credit Corporation herein referred to was organized under the federal statutes and has been in existence for many years.

"Since the organization of the Tennessee Burley Tobacco Growers' Association, the chief defendant herein, the association has grown and prospered and at the time of the filing of this suit had approximately $563,000.00 in cash on hand. This was for the most part equities from the sale of tobacco by the association.

"This suit was filed by a small number of the members of the Tennessee Burley Tobacco Growers' Association who claimed to represent themselves and a total of 7,183 members who are farmers and tobacco producers. Since this is approximately 10% of the total number of members, we may refer to the complainants herein as the minority group and the others as the majority group. The complainants, however, have in argument and briefs insisted there are many more who desire to be represented as complainants.

"Even though the association has prospered there has developed within the last few years an irreconcilable conflict between the minority group, represented by the complainants, and the majority group which includes the management and a majority of the directors. This has come about mainly because of the refusal of the defendant association and the management to pay to the farmers and members equities received by the association from the sale of tobacco for the years 1946, 1947, 1948 and 1949. It is not necessary here, it would seem, to set out in detail the methods of operation of the association or of the Commodity Credit Corporation in administering the loan support program. Every substantial tobacco grower as well as business men, judges and lawyers are somewhat familiar with the procedure and all of us are familiar, at least in a general way, with the loan support program as administered by the federal government on tobacco and other crops. The detailed procedure is not in question and is not pertinent to the issues here.

"Our Federal government has for many years been interested in seeing that the farmers, and especially tobacco growers receive a fair price for their tobacco. With that in mind the Congress created the Commodity Credit Corporation and the Commodity Credit Corporation deals with the various associations over the country which in turn deal with the farmers and warehouse men. Each year the Commodity Credit Corporation enters into a written contract with the organizations of the various states and communities which handle the loan support program and in Tennessee with the defendant Tennessee Burley Tobacco Growers' Association, setting out in detail the terms of making the loans to the association with which the association can guarantee that the farmers will receive the loan support price for tobacco.

"For each of the years involved such a contract was entered into providing how the loans were to be made, how they were to be secured, repaid, etc. and each one of these contracts contained a provision substantially as follows:

> "'All net gains accuring [sic] from the sale of tobacco upon which Commodity has loan funds under this

agreement shall be distributed on a fair and equitable basis to growers by the association, unless a disposition of such gains other than by distribution by growers is requested by the association and approved by Commodity.'

"One of the two chief questions involved in this case can be determined by an interpretation of the foregoing provision of the contract.

"Each of the approximately 76,000 members of the Association have paid the original membership fee of $3.00. In addition to that, each member who has sold tobacco has paid a certain amount to the association for the handling of the tobacco. There is no question but that these membership fees as well as charges for the handling of the tobacco belong to the association and after the cost of operation the remainder could be handled and disposed of as directed by the directors as they see fit so long as they stay within the by-laws and within the statutes of the state and the federal government.

"For the years 1946, 1947, 1948 and 1949 there was a considerable amount of tobacco handled by the defendant association. Loans were made by the federal government under the loan support program and each of the farmers were paid the minimum price or the price set by the agents of the Commodity Credit Corporation and the tobacco so failing to bring the loan support price on the floor of the warehouse was held by the association after payment to the grower of the support price, until the association was able to sell it for a price usually more than the floor price and left an equity for the owners of the tobacco.

"All of the tobacco for these years had been sold long before the filing of this bill and the minority group of stockholders insisted that their funds should be distributed to them in cash. The defendants herein do not believe that these funds should be distributed in cash but that said funds should be held by the association and used by it as a revolving fund. So, the question is, as finally admitted by counsel on both sides, can the association use these equities as a revolving fund or for the purpose of building and maintaining a redrying plant or should these funds be distributed in cash to the farmers? The answer to this question involves an interpretation of the provision in the contract herein before referred to.

"In the final arguments counsel on both sides frankly admitted that it is the purpose of the association to build and maintain a redrying

plant and to use part or all of these funds for this purpose. This was not admitted so freely at the time the suit was instituted or for some time thereafter.

"While the defendants insist that the complainants cannot take advantage of that provision in the contract between the Commodity Credit Corporation and the association, the Court is of opinion that it should be considered and is determinative of the main issue in this case if it can be properly interpreted.

"The defendants admit in their brief that the word 'distribution' can be used in more than one sense and can carry different shades of meaning. The complainants insist that there is no way the equities could be distributed except on a 'cash basis'. The lawyers, of course, disagree on this. In addition to that, each side has taken depositions of men who have been connected with the Commodity Credit Corporation at Washington and these men differ on the construction of this provision of the contract. Since the lawyers differ - and it is proper to state that they are among our best lawyers - and since the authorities from the Commodity Credit Corporation differ on the proper interpretation and since there is no precedent in Tennessee to follow; and since this Court cannot be certain as to the correct interpretation, the Court does believe that the proper solution is to decide the case upon the equities and the justice of the case without a strict interpretation of the provision of this contract.

"When the association was organized it was understood that whatever equity the farmers had left after the sale of each year's crop would be paid to the farmers in cash. For the first few years this was done. The farmers believed and understood that the membership fee of $3.00 plus the other service charges would be sufficient to bear all of the expenses of the operation of the association.

"It would not be equity or justice for the majority members of this association to take the funds that belong to the minority members over the objection of said minority group and put these funds into a redrying plant or to distribute the money in any way other than by cash. All the way through the contract of the Commodity Credit Corporation with the association and under all of the laws, both federal and state, it can be seen that the main purpose has been to protect the individual farmers in the growing and marketing of their tobacco. The association directors and their representatives have made many speeches to groups of farmers in which they told the farmers or led them to believe that their equities would be paid to them in cash; they have written letters to that effect; they have run advertisements to that effect. The defendant, H. S. Duncan, testified in this case that the money belonged to the farmers. Both the witnesses Gordon and Loos,

former government representatives, testified the same, in effect. Some of our federal courts have held that these measures are intended primarily to benefit the producers. Certainly the ordinary farmer would construe this contract to mean that he had a right to his equity in cash. So, the just and equitable thing is for those farmers who desire to have their funds or equities paid to them in cash, to receive same in cash; and it would also be equitable and fair for those who desire to leave their money in the association as a revolving fund, or to use it for the building and maintenance of a redrying plant to do so, and the Court holds that this may be done.

"The Court also holds that the association has the right to handle all of its monies as the directors see fit so long as it stays within the provisions of the by-laws and constitution and within the laws laid down by our state and federal governments, and the contracts between the Commodity Credit Corporation and the association and between the association and the farmers. But the equities held by the association belongs [sic] to the farmers and not to the association. The association acts as the agent for the Commodity Credit Corporation in making the loans and the association holds the equities until the proper time for distribution as an agent or trustee of the farmers.

"Such a distribution of the assets to the approximately 10% who desire their funds in cash will not hinder or deprive the others of the right to build and maintain a redrying plant or handling their funds as they see fit. If as the defendants claim, there is only about 10% of the farmers who desire the distribution of their equities in cash, it will still leave approximately 90% of the funds in the hands of the association, which is more than sufficient to build the redrying facilities.

"This case is referred to the Clerk & Master who will determine and report:

> (1) which members of the association desire to have their funds paid to them in cash, and
>
> (2) which members desire to have their funds left with the association to be used as a revolving fund or as directed by the directors.

"This may be done by letters to the various members, and replies mailed to the Clerk & Master.

"The Court is not overlooking the marketing agreement between the farmers and the association, but even if these parties could disregard the contract between Commodity Credit Corporation and the association and go beyond its terms the farmer-association contract did not contemplate using the equities to finance a redrying plant. Perhaps, by placing a strained construction on this contract, it could be so construed, but it must be interpreted in the light of all the facts and circumstances. The record is convincing that such was not the intention of the farmers at the time the contracts were signed.

"The injunction heretofore granted will be modified to the extent that the association will pay to the Clerk & Master a sum sufficient to mail and print the letters. The association will also furnish the Clerk & Master a complete list of members with addresses. Other compensation of the Master will be reserved until further order.

"The Tennessee Association is the only agency handling the price support program for tobacco that does not reconize [sic] the obligation to pay the equities in cash. The Commodity Credit Corporation never at any time approved any distribution other than by cash.

"By the original and amended bill, the complainants also seek a recovery from the defendants for illegal and improper use of the funds of the association and also seek to enjoin the association and its directors from expending money for any construction other than the buildings already started.

"This Court cannot find that there has been such waste or mismanagement by the association or any officers thereof to justify a recovery. While it may be true that some of the expenses have been somewhat higher than most farmers would like, the Court cannot find and does not find that they have gone beyond the provisions as set out by the by-laws and the constitution or the law. These expenditures have been approved by the board of directors and in the handling of $33,000,000.00, as has been done by this defendant association, it would be almost impossible to do so without finding some small item or items which were not handled perfectly. There is bound to be some discrepancies and irregularities. These discrepancies and irregularities were minor and do not justify a recovery against the defendants.

"If either the complainants or the defendants, or both, desire an appeal, the Court will be inclined in its discretion to grant said appeal at this time, even before a reference.

"Other than as herein before stated, the injunction is dissolved.

"The costs of this cause will be paid one-half by the complainants and one-half by the defendants."

FLOWER GROWERS' COOPERATIVE SUBJECT TO CERTAIN CIVIL AERONAUTICS ACT REQUIREMENTS

(Consolidated Flower Shipments, Inc. - Bay Area v. Civil Aeronautics Board, C.A. 9th, _____F. 2d _____)

In this case, decided June 9, 1954 (see 22 L.W. 2617), the Ninth Court of Appeals held this flower growers' shipping cooperative subject to the Civil Aeronautics Act's certification requirement for air freight forwarders and to the Civil Aeronautics Board's freight forwarder regulations.

The court pointed out that the Civil Aeronautics Act contained no exception similar to that found in the Interstate Commerce Act. Nor would the court go along with the cooperative's argument that it was not a "public" carrier, since the evidence showed that its services seemed to be open to all who would join. Finally, the court would not ignore the separate legal entity of the cooperative and regard it merely as the alter ego of the flower producers members; a viewpoint advanced on behalf of the cooperative.

PAYMENTS TO QUALIFIED COOPERATIVES UNDER NEW YORK MILK ORDER HELD VALID

(Grant v. Benson, (D.C.) _____F. Supp._____)

Payments to qualified cooperatives from the "milk pool" as provided under the milk order for the New York milk marketing area were held to be (1) necessary to pay for certain market-wide services performed by the cooperatives which benefited members and nonmembers alike and (2) a reasonable means of arriving at a "uniform price." A temporary injunction had been entered on April 7, 1952, under which approximately a million and a half dollars had been placed in escrow by the Marketing Administrator. The court denied a permanent injunction and dismissed the suit. However, it is understood that the case will be appealed.

Grant and five other producers in the area filed a complaint to restrain the Secretary of Agriculture from distributing the cooperative payments in question. The payments were made pursuant to regulations (7 C.F.R. 927.76) duly promulgated under the Agricultural Marketing Agreement Act of 1937, as amended (7 U.S.C. 601 et seq.).

"The milk is classified as to price by the Administrator appointed by the Secretary of Agriculture on the basis of the use made of it. The milk prices are averaged out by the Administrator monthly. The handlers of milk in the higher use classifications pay to the Market Administrator an amount when the price received from the sale of milk is above the blended uniform price. The fund so accumulated is called the 'Producer Settlement Fund' or 'Milk Pool'. The Administrator pays out of the producer settlement fund to the handlers of the milk in the lower use classifications so that all handlers in turn pay the producers a uniform price for their milk regardless of how the milk is used.

"By Sec. 927.76 (Federal Order No. 27) the Market Administrator deducts from the producers settlement fund at least 2¢ per hundredweight for all milk marketed by the members of each qualified cooperative. These amounts are paid to the qualified cooperative associations for market-wide services. Plaintiffs have never been members of any qualified cooperative association."

The plaintiffs claimed theirs was a class action, which defendants denied. Although the court was "inclined to believe" it was a class action, it did not decide this issue since it was conceded that

plaintiffs had a right to a determination of the validity of the regulations because of their pro rata interest in the fund.

It was stipulated that the constitutionality of neither the State nor Federal Act was involved, so the court was "entirely confined . . . to the validity of the Federal Order although taking into consideration that it is a joint order and a joint pool held by the Administrator acting under the Federal Act and also the New York State Act."

Excerpts from the court's decision on this issue follow:

> "This court is of the opinion that the New York State Act has no effect or consequences upon the Federal Order, and that the Federal Order must stand or fall under 7 U.S.C.A. Sec. 601 et seq. Defendants lean upon Sec. 610 (1) for validity of the federal regulations. In view of the limitations in that section 'to issue orders (subject to the provisions of Section 608c of this title)' no strength is given to defendants' position. Even if it is a federal-state order expressly provided for by the New York State Law, it must depend on the federal statute for its validity in this proceeding.
>
> "The defendants also seek authority for the deductions to be paid to qualified cooperatives under Section 608c (5) (B)(ii)(d) which reads as follows:
>
> > "'A further adjustment, equitably to apportion the total value of the milk purchased by any handler, or by all handlers, among producers and associations of producers, on the basis of their marketings of milk during a representative period of time.'
>
> "It is to be observed that the adjustment is to be on the basis of marketings of milk by all producers, but not upon market-wide services performed by qualified cooperatives as provided for in the order and objected to by the plaintiffs.
>
> "This proceeding is not de novo. This court may not substitute its judgment for the Secretary's findings of fact and conclusions thereon, where the findings of fact are supported by substantial evidence. National Broadcasting Company v. United States, 319 U.S. 190; Universal Camera Corp. v. Labor Bd., 340 U.S. 474. The court, therefore, must turn to the findings of fact made by the Secretary and rely upon them in determining the validity of the order.

"The Secretary made findings of fact based upon substantial evidence in the record."

* * * * * *

(Here the court set forth at considerable length the findings of the Secretary.)

"In the light of these findings Sec. 608c (5)(B)(ii) must be examined. It provides:

> "'for the payment to all producers and associations of producers delivering milk to all handlers of uniform prices for all milk so delivered, irrespective of the uses made of such milk by the individual handler to whom it is delivered;'

"The very foundation of the Act as a whole is to secure a uniform price to all milk producers. The entire purpose of the Act fails if members of qualified cooperatives receive a lower price for their milk than non-members. Without the payment for the required market-wide services performed by the qualified cooperatives, there would exist a disparity in the blended price received by members of qualified cooperatives and non-members. These services require the employment by each qualified cooperative of an economist, lawyer, field supervisor, editor, fieldman and other personnel. The Secretary found that the services cost at least as much as the payments made to the qualified cooperatives, and the members of such cooperatives still pay for all other activities of the cooperatives. These services were found to be necessary to effectuate the other provisions of the order. In other words in order to obtain a uniform blended price to producers from which the specified adjustments may be made as provided by the statute, in the first instance, a uniform price to all producers is required by the statute.

"It is to be noted that Sec. 608c (5) provides:

> "'In the case of milk and its products, orders issued pursuant to this section shall contain one or more of the following terms and conditions, and (except as provided in subsection (7) of this section) no others:'

"Therefore, to not deduct the amount paid to qualified cooperatives would be inconsistent with the very wording of the statute and would violate the 'following terms and conditions' which require uniform prices to all producers and associations of producers for their milk. While Congress did not spell out the exact language or authority for the Administrator to make these deductions it certainly specified in no uncertain terms that one of the conditions should be a uniform blended price for all milk produced in the area. Congress wisely left to the Administrator the mechanics of arriving at a uniform price; provided, that this uniform price was paid to all producers of milk.

"Brannan v. Stark, 342 U.S. at the bottom of page 463 makes this very distinction and indicates that if the services to non-members of qualified cooperatives are compulsory, then the price by virtue of the contribution by all members from the 'milk pool' to the fund for the payment of qualified cooperative producers in fact would equalize or become uniform. Inasmuch as the former regulation required compulsory services by the qualified cooperatives for the utilization of milk as stated by the Supreme Court Opinion at footnote 12, and the amended order also requires certain compulsory market-wide services, and the payments to the qualified cooperatives merely pay for these services which are of benefit to the non-members a uniform price to all producers and associations of producers of milk results.

"The Secretary further found and concluded that the payments to qualified cooperatives (the terms and conditions in the amendments) are incidental to, and not inconsistent with, the terms and conditions specified by subsection (5) - (7) of Sec. 608c and necessary to effectuate the other provisions of the order. These are an interpretation of the Act or conclusions of law that are subject to review by this court. Administrative Procedure Act, Sec. 10 (e) (5 U.S.C.A. 1009 (e)). However, weight may be given to the construction of the statute by the Secretary. United States v. Jackson, 280 U.S. 183; United States v. Citizens Loan Co., 316 U.S. 209; Labor Board v. Denver Bldg. Council, 341 U.S. 675, 691, 692. I do place some weight to the Secretary's interpretation of the Statute, considering the findings of fact which were based upon substantial evidence."

RIGHTS OF STOCKHOLDERS WITH RESPECT TO CHOICE OF DIRECTORS

(Lazar v. Knolls Cooperative Section No. 2, 130 N.Y.S. 2d 407)

In this case a stockholder of the cooperative apartment corporation asked for an order requiring the officers of the corporation to call a stockholders' meeting for the election of directors or to consider his demand for the removal of directors. The court held the stockholder was entitled to this relief.

The facts are summarized in the opinion in part as follows:

> "The defendant, The Knolls Cooperative Service No. 2, Inc. (to which I will refer as 'the corporation'), is a cooperative corporation and the plaintiff is one of its stockholders. It entered into an agreement with Knolls Construction Company (to which I will refer as 'the partnership') for the construction of a cooperative apartment house building for the corporation. . . .
>
> "The corporation made a mortgage to the defendant, Dry Dock Savings Bank, and the bank advanced most of the money due under the mortgage to the corporation as the construction progressed. The corporation, in turn, paid most of the money advanced to the partnership. Construction has neared completion and a closing date will soon be fixed for the payment of the last advance by the bank to the corporation. The plaintiff believes this amount will be paid over to the partnership. Prior to the fixing of a closing date, the corporation's board of directors must adopt a resolution to the effect that the buildings have been substantially completed by the partnership.
>
> "By reason of various business associations there is a close relationship between the officers and directors of the corporation and the members of the partnership. . . . None of the individual defendants are stockholders, and only stockholders may occupy apartments in the cooperative building. Those defendants who are directors were designated as such in an amended certificate of incorporation filed on or about August 11, 1952. No stockholders' meeting has been held for an election of directors.
>
> "The plaintiff expresses a fear that representation by the individual defendants of identical interests may result in

an improper inspection of the cooperative building. He claims that a board of directors should be elected by the stockholders who are going to live in the building to ascertain that construction conforms to the plans and specifications. He states that unless the final payment by the defendant bank is enjoined, a board of directors representative of the stockholders will not have an opportunity to make a genuine determination as to whether the partnership performed the construction agreement.

"The plaintiff pleads a second cause of action in which he incorporates the facts which I have summarized and also alleges that a proper demand was filed for the removal of the defendant directors with the secretary of the corporation pursuant to Section 63 of the Cooperative Corporations Law, and that the defendants have failed to call a stockholders' meeting to consider the charges contained in the demand."

After disposing of the defendants' claim that the suit was not properly brought as a derivative action by holding this was a "representative," as distinguished from a "derivative," action, the court said:

"Management of a corporation may be in skilled hands; its policies may be in the best interests of the corporation; there may be no waste or wrongdoing of any kind in so far as the corporate interests are involved; and yet the stockholders may attack the right of the directors to act as such.

"Section 11 of the Cooperative Corporations Law requires that a certificate of incorporation state the names and post office addresses of the incorporators and the names and post office addresses of the directors until the first annual meeting. There is an implication in the phrase 'until the first annual meeting' that such directors are intended to act only until such time as the stockholders are able to function and elect directors. In this case, the individual defendants are, with one exception, both the incorporators and directors named in the certificate. Compliance with the statute requires that they hold the first annual meeting within a reasonable time so as to give the stockholders an opportunity to elect their own board as promptly as possible. They are not supposed to perpetuate themselves in office despite the wishes of the stockholders.

"The amended certificate of incorporation was filed on August 11, 1952. Under Article I, Section 1 of the by-laws an annual meeting of stockholders for the election of directors was to be held on June 6, 1953. The plaintiff has shown prima facie some need for such a meeting. Neither that nor a showing of any wrongful acts in management of corporate affairs is a necessary condition precedent for holding a meeting which is required by the by-laws. The same principle applies with respect to the filing of charges for the removal of directors pursuant to Section 63 of the Cooperative Corporations Law. Under that section a meeting must be held promptly to act on such charges. These charges were filed on January 25, 1954 but no meeting has been held.

"The second cause alleged in the complaint certainly states a cause of action and the motion to dismiss is denied.

"In support of the motion for an injunction pendente lite, the plaintiff in substance states the facts pleaded in the complaint, and points to the fact that in a somewhat similar transaction with respect to The Knolls Cooperative Section No. 1, Inc., and the Knolls Construction Company, the stockholders who took control of the cooperative corporation after completion of construction found to their serious damage that there had not been compliance with the construction contract. Many of the same defendants involved in this transaction were involved in the former one, and there was a similar interlocking of interests between the corporation and the partnership.

"The defendants urge that the stockholders have sufficient protection in regard to the performance of the construction contract as a result of governmental supervision. That is for the stockholders or for a board of directors elected by them to determine. The defendants also urge that no meetings of the stockholders have been called pursuant to the by-laws and in response to the plaintiff's charges under Sec. 63, Cooperative Corporations Law, because in the opinion of the present directors (who were not elected), it would serve the stockholders' interests best to wait to elect directors until they have moved into their apartments and become familiar with the building and its operations. That, too, is a matter for the stockholders to determine. A stockholder cannot be made to accept generous considerations in exchange for his rights under the law.

"The defendants have been in continuous violation of the law of this state and of the by-laws of the corporation in neglecting to call both the annual meeting and the meeting to hear the charges. They cannot take advantage of this delay by informing this Court that if the delay is continued just a little longer, they will complete their work with the bank and the partnership. I appreciate that there is need for not delaying this project and I will endeavor to minimize any delay, but I am not going to permit the plaintiffs' rights to be violated simply for the sake of speed.

"Section 14 of the Cooperative Corporations Law makes the corporation laws of the state applicable to cooperative corporations, except where there is a conflict in provisions. Section 63 of that law contains no provision for enforcing the holding of a meeting promptly where the directors fail to call one at all. Article 6 of the General Corporation Law vests the court with sufficient power to compel the holding of a meeting required by law where there is a prima facie showing for the need of such a meeting and the only reason for not calling it is a desire by directors, not elected and against whom charges are pending, to continue themselves in office. Such a meeting will be ordered to be held within ten days after the settlement of an order. Until that meeting is held, the temporary injunction will be granted.

"With respect to the failure to call the annual meeting, the defendants are directed to call one as promptly as possible. Until such meeting is held and a board is elected, the temporary injunction will remain in effect. If delay is caused, it has been caused by the present directors' failure to comply with the law. If they wish to avoid further delay, they can do so by calling the meetings promptly."

SOUTH CAROLINA REA COOPERATIVE HAS TORT IMMUNITY

(Byrd v. Blue Ridge Rural Electrical Cooperative, U.S.D.C., W.D.S.C., 118 F. Supp. 868)

In a negligence suit against the defendant, a nonprofit membership cooperative operating under the South Carolina Rural Electric Cooperative Act, the court held the defendant immune from liability for torts of its agents and servants. This ruling was sustained on appeal.

The Supreme Court said, in part:

> "The question of the liability of a charitable institution to respond in damages for the negligence of its employees, agents and servants has been before the South Carolina Courts on several occasions. Regardless of what the rule in other jurisdictions may be the question has been settled in South Carolina by the adoption of the rule of full immunity of such institutions from the torts of their agents and servants. Lindler v. Columbia Hospital, 98 S.C. 25, 81 S.E. 512; Vermillion v. Woman's College of Due West, 104 S.C. 197, 88 S.E. 649; Peden v. Furman University, 155 S.C. 1, 151 S.E. 907; Caughman v. Columbia Y.M.C.A., 212 S.C. 337, 47 S.E. 2d 788.
>
> "The reason for the rule was clearly stated in Vermillion v. Woman's College of Due West, 104 S.C. 197, 88 S.E. 649, and recently quoted with approval by Mr. Justice Oxner in Caughman v. Columbia Y.M.C.A., 212 S.C. 337, at page 344, 47 S.E. 2d 788, 790, as follows:
>
> > "'* * * The exemption of public charities from liability in action for damages for tort rests not upon the relation of the injured person to the charity, but upon grounds of public policy, which forbid the crippling or destruction of charities which are established for the benefit of the whole public to compensate one or more individual members of the public for injuries inflicted by the negligence of the corporation itself, or of its superior officers or agents, or of its servants or employees. The principle is that, in organized society, the rights of the individual must, in some instances, be subordinated to the public good. It is better for the individual to suffer injury without compensation than for the public to be deprived of the benefit of the charity. The law has always favored

> and fostered public charities in ways too numerous to mention, because they are most valuable adjuncts of the state in the promotion of many of the purposes for which the state itself exists.'

"The defendant is a non-profit membership cooperative organized and operating under the provisions of the South Carolina Rural Electric Cooperative Act, Sections 12-1001 et seq. of the Code of Laws of South Carolina, 1952. This statute was passed as a result of and to take advantage of the Federal Rural Electrification Act, 7 U.S.C.A. §§ 901-914, which provided financial assistance in the form of long-term loans at favorable interest rates to local rural electric cooperatives.

* * * * * *

"In Bookhart v. Central Electric Power Coop. Inc., 219 S.C. 414 at page 421, 65 S.E. 2d 781, 783, the Supreme Court of South Carolina said: 'As pointed out in the judgment under review, the need of available electric energy in rural, farm areas, of which this State is chiefly composed, was compelling and the great progress by which it has been met since the passage of the law is common knowledge.'

"Under the South Carolina statute, such cooperatives are exempt from regulation by the Public Service Commission. . . . It is obvious that such cooperatives have a special and favored position under the South Carolina statutes.

"The defendant Blue Ridge Rural Electric Cooperative is a nonprofit cooperative and no one derives any profit from its operation. Greene County Rural Electric Cooperative v. Nelson, 1944, 234 Iowa 362, 12 N.W. 2d 886. As a nonprofit cooperative performing a laudable purpose in which the public and the State are interested, every reason given by the South Carolina Court in Vermillion v. Woman's College of Due West, supra, for exemption from liability for tort applies. The same rule which applies to a hospital, a woman's college or a Y.M.C.A. should likewise apply to a Rural Electric Cooperative. The Arkansas Court applied the same rule in the case of Arkansas Valley Co-Op. Rural Electric Co. v. Elkins, 200 Ark. 883, 141 S.W. 2d 538, where it was specifically held that a nonprofit-sharing rural electric cooperative created under a statute similar to the South Carolina statute could not be held liable in damages for injuries resulting from a tort of one of its employees in the absence of a statute providing for such liability. There is no such statute in South Carolina."

REA COOPERATIVE DOES NOT HAVE EXCLUSIVE FRANCHISE RIGHT IN AREA SERVED

(Sheridan County Electric Co-op, Inc. v. Montana-Dakota Utilities Co. 270 P. 2d 742)

Plaintiff, an electric cooperative organized under the Montana Rural Electric Cooperative Act, sought to enjoin defendant from constructing an electric distribution line in areas served by plaintiff. A demurrer to the complaint was sustained and plaintiff appealed. The Supreme Court held that the Montana Act did not give plaintiff an implied exclusive franchise right in areas which it served.

Pertinent excerpts from the opinion follow:

> "The controlling question raised by the demurrer is: Does the plaintiff have, as alleged in the complaint, 'an implied exclusive franchise right * * * sanctioned and authorized by the laws of the State of Montana' to furnish electric energy to such rural areas whereby defendant would be prevented from competing therein?
>
> "To determine this question reference must be had to the Rural Electric Cooperative Act, R.C.M. 1947, §§ 14-501 to 14-531, under which plaintiff was organized and created * * *
>
> "Under the provisions of this Act the plaintiff has a right to provide electric energy to the designated rural areas. Nowhere in said Act, however, can one find anything which, by express words or by implication, indicates that the legislature intended to give an exclusive right to plaintiff to furnish electric energy in such rural districts. To the contrary, the plain wording of R.C.M. 1947, § 14-503, indicates the opposite intention and limits the right of plaintiff to provide electric energy, in such rural areas, to certain users, section 14-503 providing: 'A cooperative shall have power: * * * (d) To generate, manufacture, purchase, acquire, accumulate and transmit electric energy, and to distribute, sell, supply and dispose of electric energy in rural areas to its members, to governmental agencies and political subdivisions, and to other persons not in excess of ten per centum (10%) of the number of its members'.

"Had our law makers intended that cooperatives should have the exclusive right to furnish electric energy in such rural areas, and thus prevent competition by other authorized electric public utility, they should have used clear and apt words to so declare. Certainly, no such far-reaching right can be left to implication or inference."

RECENT INTERNAL REVENUE SERVICE RULINGS OF INTEREST TO COOPERATIVES

Rev. Rul. 54-244 (1954 Int. Rev. Bull. No. 26 at 5)

"The taxpayer has obtained the majority of the capital stock of a growers' marketing cooperative association which was incorporated in the State in which it operates and which has been held to be exempt for Federal income tax purposes under the provisions of section 101 (12) of the Internal Revenue Code. The taxpayer proposes to liquidate the corporation. The books of the association show no earned surplus but there is capital stock outstanding which was issued to growers pursuant to a revolving fund agreement. In accordance with such agreement the association each year retained portions of amounts due growers for crops and issued stock therefor having par value equal to the retained portion. The association then used such retentions in its business. Growers have reported the face amount of the stock received as part of income from crops each year. Held, that the value of the above-described stock does not represent earnings and profits of the association within the meaning of section 112(b)(7)(E) of the Code."

Rev. Rul. 54-297 (1954 Int. Rev. Bull. No. 31 at 10)

"Advice is requested as to the proper treatment of amortization of emergency facilities and Federal income taxes in the determination of the maximum allowable exclusion for patronage dividends in the case of a nonexempt cooperative association.

"A 'cooperative association,' as that term is defined in section 39.101(12)-2(b)(1) of Regulations 118, includes, with certain exceptions, any corporation operating on a cooperative basis and allocating amounts to patrons on the basis of business done with or for such patrons. The Internal Revenue Service has consistently held that such associations, even though not exempt from taxation, may exclude from gross income certain amounts returned to their patrons as true patronage dividends. See I. T. 1499, C. B. I-2, 189, and A. R. R. 6967, C. B. III-1,287.

"Section 23 of the Internal Revenue Code provides that in computing net income there shall be allowed as deductions all ordinary and necessary expenses paid or incurred during a taxable year including, among other things, a reasonable allowance for depreciation. Since the deduction for amortization of emergency facilities provided for in section 124A of the Code is in lieu of the deduction for depreciation allowable under section 23(l) of the Code, such deduction should

be used in the determination of 'net income' for the purpose of computing the maximum amount of patronage dividends that may be excluded from gross income in the case of a nonexempt cooperative association under the rule set forth in A. R. R. 6967, supra.

"In Farmers Union Cooperative Exchange v. Commissioner, 42 B. T. A. 1200, (appeal dismissed), 122 F.(2d) 718, acquiescence C. B. 1944, 8, it was held that for the purpose of determining the maximum allowable exclusion for patronage dividends in the case of a nonexempt cooperative association under the rule set forth in A. R. R. 6967, supra, the 'net income' of the association should not be reduced by Federal income taxes.

"During the year 1917 refunds were paid to members of the cooperative considered in A. R. R. 6967, supra, in the amount of 39.16x dollars. That ruling holds, in effect, that the amount available for refund consists of that proportion of the net profits, after deducting the fixed dividend on outstanding capital stock, which the amount of business transacted with members bears to the entire amount of business transacted. Up to the amount available for refund thus computed, a distribution by a cooperative association to its members, upon the basis of the business transacted with them will be deemed to be a true patronage dividend, excludable by the association in computing its taxable net income for Federal income and profits tax purposes. This holding is based on the assumption that the dealings with members and nonmembers are equally profitable. Applying this rule to the facts there involved the following computation was set forth:

		Dollars
"Net income per agent's report		73.93x
Deduct: Interest at 8 percent on capital stock--		
97.96x (12 months)	7.84x	
.68x (11-1/2 months)	.05x	
24.36x (4-1/3 months)	.7 x	
		8.59x
Profits from nonmembers' business plus amount available for refund --		65.34x
Total business (members and nonmembers)		4,642.83x
Business transacted with members		3,056.04x
Percentage of members' business to total business transacted		65.82
Available for refunds to members (65.34x dollars x 65.82 percent)		43. x

"Therefore, inasmuch as but 39.16x dollars was distributed to members during the year 1917 as patronage dividends, which amount is less than the amount available for distribution as above computed, the full amount of 39.16x dollars should be allowed as an exclusion for 1917.

"Accordingly, it is held that the deduction for amortization of emergency facilities, where an election has been made under section 124A of the Internal Revenue Code, must be taken into consideration in computing the 'net income' of a nonexempt cooperative association for the purpose of determining the maximum allowable exclusion for patronage dividends under the rule set forth in A. R. R. 6967, supra, described above. Federal income taxes paid by the association should not be taken into consideration in making this determination."

Rev. Rul. 54-305 (1954 Int. Rev. Bull. No. 32 at 7)

"Advice is requested whether a corporation organized and operated for the primary purpose of operating and maintaining a purchasing agency for the benefit of its otherwise unrelated members who are exempt from Federal income tax as charitable organizations, is itself exempt from Federal income tax under the provisions of section 101 of the Internal Revenue Code.

"The purposes of the instant organization are to secure for hospitals and other charitable institutions the advantages of cooperation in establishing uniform standards as to quality and kind of supplies and the purchasing of the same in accordance with definite specifications and agreements; also to promote the economical and efficient administration of hospitals and other institutions and to establish and maintain a central purchasing agency. Any hospital or similar institution not conducted for profit and engaged in whole or in part in charitable work is eligible for membership. The organization's income is derived from dues, cash discounts on purchases for members, and service charges. Substantial profits are realized by the organization from these operations. Only a portion of such profits are distributed by the organization to its members.

"Section 101 of the Code provides in part that:

> "'An organization operated for the primary purpose of carrying on a trade or business for profit shall not be exempt under any paragraph of this section on the ground that all of its profits are payable to one or more organizations exempt under this section from taxation. * * *'

"Section 39.101-2 of Regulations 118 construing such section of the law provides in part that if a subsidiary organization of a tax-exempt organization would itself be exempt on the ground that its activities are an integral part of the exempt activities of the parent organization, its exemption will not be lost because, as a matter of accounting between the two organizations, the subsidiary derives a profit from its dealings with its parent organization, for example, a subsidiary organization which is operated for the sole purpose of furnishing electric power used by its parent organization, a tax-exempt educational organization, in carrying on its educational activities. However, the subsidiary organization is not exempt from tax if it is operated for the primary purpose of carrying on a trade or business which would be an unrelated trade or business (that is, unrelated to exempt activities) if regularly carried on by the parent organization. For example, if a subsidiary organization is operated primarily for the purpose of furnishing electric power to consumers other than its parent organization (and the parent's tax-exempt subsidiary organizations), it is not exempt since such business would be an unrelated trade or business if regularly carried on by the parent organization. Similarly, if the subsidiary is owned by several unrelated exempt organizations, and is operated for the purpose of furnishing electric power to each of them, it is not exempt since such business would be an unrelated trade or business if regularly carried on by any one of the tax-exempt organizations.

"In determining whether an organization is subject to tax under the Federal statutes the facts involved in each case must be carefully considered. In the instant case the activities of the organization concerned consist primarily of the purchase of supplies and the performance of other related services for the several otherwise unrelated charitable organizations that constitute its membership. It is apparent that such activities in themselves cannot be termed charitable, but are ordinary business activities.

"Under the provisions of section 101 of the Code an organization which is operated for the primary purpose of carrying on a trade or business for profit is not exempt from Federal income tax, notwithstanding that any profits derived are payable to one or more exempt organizations. Furthermore, under the regulations which interpret such section, it is clear that a corporation formed to service several tax-exempt organizations is not itself exempt if the services performed would be unrelated activities if carried on by any one of the tax-exempt organizations served.

"Accordingly, it is held that a corporation organized and operated for the primary purpose of operating and maintaining a purchasing agency for the benefit of its otherwise unrelated members, who are exempt from Federal income tax as charitable organizations, is engaged in business activities which would be unrelated activities if carried on by any one of the tax-exempt organizations served. Therefore, the corporation is not entitled to exemption under section 101 of the Internal Revenue Code."